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SUBJECT: KAZAKHSTAN: UNDER SECRETARY BURNS'S JULY 10 MEETING WITH
PRIME MINISTER MASIMOV FOCUSES ON WTO ACCESSION

REF: ASTANA 1145

11. (C) SUMMARY: In a July 10 meeting in Astana with Prime Minister Karim Masimov, Under Secretary of State Bill Burns urged Kazakhstan to continue its bilateral WTO accession negotiations and not to close any doors, even if Astana is currently focusing on the Russia-Belarus-Kazakhstan (RBK) Customs Union. After summarizing Kazakhstan's economic path since independence in 1991, Masimov reviewed Kazakhstan's response to the global financial crisis and judged that it will emerge from the crisis intact, unless there are further earthquakes to come. The Kazakhstani interlocutors were nonplussed when asked if Belarus would not hold back Russia, and especially Kazakhstan, from joining the WTO, if the three try to join as a customs union. In the end, the Kazakhstanis offered that they hoped to play a positive role between Moscow and Minsk, and expected that the other two governments would accept Kazakhstan's more progressive economic and financial models. END SUMMARY.

12. (C) After Under Secretary Bill Burns's initial comments to Prime Minister Karim Masimov on the July 6-7 Obama-Medvedev summit in Moscow and the G-8 meeting in L'Aquila, Italy, he and Masimov focused on Kazakhstan's June 9 decision, announced in Moscow, to suspend its World Trade Organization (WTO) accession negotiations in favor of creating a Russia-Belarus-Kazakhstan (RBK) Customs Union. Burns said, "I hope you can think creatively and flexibly about keeping your bilateral accession negotiations going, even while pursuing the customs union."

COMING THROUGH THE GLOBAL FINANCIAL CRISIS

13. (C) Masimov hewed to his prepared talking points and stated, "Kazakhstan and the United States always have been, are now, and will continue to be good friends." Reviewing Kazakhstan's economic and financial situation, he noted that his country had been hit hard by the liquidity crunch of the global financial crisis a year earlier, in August 2007, than the rest of the world, because Kazakhstan's private-sector banks are embedded in the global economy and had succumbed to exceptionally high levels of foreign borrowing, especially in the construction and real estate sectors. He briefly documented Kazakhstan's close collaboration with international

financial advisers ("the same ones you use") and international financial institutions. He said, "We are fully committed to accountability and transparency." He noted that the current level of the price of oil is helping Kazakhstan's recovery, because the country's current budget is calculated on oil at \$40 per barrel. "Every dollar above that helps us," he said.

"FAILED" BANKS' CREDITORS WILL RECOVER 80% OF INVESTMENT

14. (C) Masimov said that the government had taken over -- "I hate to say nationalized" -- two of Kazakhstan's largest private banks, Bank Turan Alem (BTA) and Alliance. He revealed that on July 9, agreement had been reached for the international creditors to recover 80% of their investments in these banks. He said that the negotiations had been so creative, transparent, and successful that they should stand as a case study for future such situations. He summarized, "If there is not another 'Lehman Brothers earthquake,' we should be okay and should see recovery and renewed growth." Burns responded that President Obama and his administration are working diligently to develop new regulatory systems. He recommended that the government of Kazakhstan stay in close touch with the U.S. government on these matters.

"RBK CUSTOMS UNION SHOULD BE ECONOMICALLY ADVANTAGEOUS FOR KAZAKHSTAN"

15. (C) Masimov deferred to Vice Minister of Industry and Trade Zhanar Aitzhanova to comment on the RBK Customs Union. She acknowledged that it will be problematic for Kazakhstan to join the WTO as part of the RBK Customs Union (see reftel), and said that the three customs union members will consult with an international law firm to find a way forward. Putting on a brave face, she asserted that 17 or 18

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customs unions already exist within the framework of the WTO. She said that she and Russia's and Belarus's WTO negotiators will next report to the WTO in Geneva in September.

16. (C) Special Assistant to the President and NSC Senior Director for Russia and Eurasia Michael McFaul asked Aitzhanova if Kazakhstan intended to continue its bilateral accession negotiations. She replied, "No, we have suspended bilateral negotiations until the path forward is clear."

17. (C) Burns offered, "Our only interest is that you keep all your options open. It would be enormously complicated to try to join as a customs union if you forego bilateral accession; it would be a long-term set-back for you." He added that if Russia and Kazakhstan were interested only in exporting their raw-material natural resources, that would be one thing, but a sophisticated diversified economy benefits from the WTO. Aitzhanova responded, "It's really a matter of timing. We want to focus on the customs union now so that our positions are clear when we are ready to accede to the WTO together."

THE REAL STORY?

18. (C) The Prime Minister said, "Let me tell you what's really behind the customs union -- it's all about our economic policy. At different stages of our independence, we have had different influences. For the first years, 1991-99, our goal was simply to survive the collapse of the Soviet economy. We listened to lots of consultants, and, without any international experience, tried to determine which were the best. If you look around Central Asia, we succeeded especially well, and now are close to Central European standards of economic and financial development. On the investment side, at the beginning, investors mostly wanted our raw materials, our oil and mineral resources. Until recently, our government stood back and took a hands-off stance. However, during 2004-07, we became increasingly concerned that our independent, private banks were overexposed in real estate and construction. But the banks said, 'That's our business, not yours.' Now, after the 2007-09 global financial collapse, we understand that new and more aggressive regulation, even state intervention, is essential. We are studying the experience of different countries and think perhaps Canada might be a useful model."

A BRAVE FACE?

¶9. (C) Returning to the issue of the RBK Customs Union, Masimov said, "When potential investors look at us, they tell us in the end, our market is too small. That's why we need to be included in the Russian market. In fact, our tax and regulatory regimes are better, more progressive than Russia's, and so, in the customs union, we expect Russia to adopt our standards. We will convince new investors to build their factories near our border with Russia." Burns said, "We respect your views and experience. We simply hope you can keep your bilateral WTO accession negotiations alive." Masimov acknowledged that the last five years of WTO negotiations have indeed helped Kazakhstan significantly. Aitzhanova added, "Our goal is to lead in the customs union, since we are more progressive in economic, financial, and trade policy than Russia."

BELARUS: THE ELEPHANT IN THE ROOM

¶10. (C) McFaul then asked, "Won't Belarus slow you down?" The Kazakhstani interlocutors fumbled at first. Masimov said he had traveled to Minsk after the June 9 announcement in Moscow of the RBK Customs Union and had been pleasantly surprised how clean the city was. After a bit of hemming and hawing, Masimov added that Belarus builds agricultural machinery that Kazakhstan needs, and it's better than what Russia produces. (COMMENT: Throughout Central Asia, Belarus's agricultural machinery is recognized as inexpensive but shoddy when compared to U.S., German, Japanese, and South Korean products. END COMMENT.) Burns commented that the U.S. concern is

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that Belarus is many years behind Russia and Kazakhstan in the WTO process.

¶11. (C) Recovering, Masimov said, "Let me tell you confidentially, Kazakhstan's and Russia's WTO negotiators have agreed to provide technical assistance to Belarus to help them leap forward in the WTO process. We hope they can cover ten years in one year. Further, because Kazakhstan has good, stable relations with both, we expect we will be able to be the conciliator between Moscow and Minsk when they have their periodic economic flare-ups, like the recent 'milk crisis.'"

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